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Message Text

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DRAFTED BY L/ARA:DAGANTZ
APPROVED BY ARA:AFISHLOW
TREASURY:FMARESCA/RGOODMAN
DIST: STATE, TREASURY, COMMERCE, CIEP
---------- 122455
P 091734Z FEB 76
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TO AMEMBASSY LIMA PRIORITY

C O N F I D E N T I A L STATE 031162

E.O. 11652: GDS
TAGS: EIND, BDIS, EINV, PFOR, PE

SUBJECT: MARCONA - TECHNICAL COMMISSION MEETING EVENING JANUARY 29

1. TECHNICAL COMMISSION RECONVENED AT 6 P.M. JANUARY 29 TO CONTINUE DISCUSSIONS OF 4 PERCENT ALLOWANCE ISSUE. THE GOP DESIGNATED EXPERT TAX JUDGE LA ROSA GAVE A LENGTHY AND LUCID REVIEW OF THE EVENTS LEADING UP TO THE GOP'S DECISION THAT THE 4 PERCENT ALLOWANCE PROVIDED FOR IN THE 1966 CONTRACT WAS NOT CONTROLLING IN DETERMINING MARCONA'S NET INCOME. HE ARGUED THAT THE 4 PERCENT FORMULA SIMPLY ESTABLISHED THE FOB PRICE FOR THE PURPOSE OF DETERMINING ROYALTIES TO BE PAID UNDER THE CONTRACT IT DID NOT DETERMINE THE EXTENT TO WHICH SALES COMMISSIONS WERE DEDUCTIBLE AS AN ORDINARY BUSINESS EXPENSE. NEVERTHELESS, HE INDICATED A MAJOR CHANGE IN THE GOP POSITION; RATHER THAN DENYING A DEDUCTION FOR THE ENTIRE 4 PERCENT C & F ALLOWANCE, THE GOP WOULD ALLOW A DEDUCTION FOR 2 PERCENT FOB AND IN ADDITION WOULD RECOGNIZE THAT THE IRON ORE BUSINESS - IN CONTRAST TO COPPER MARKETING - CONFIDENTIAL

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JUSTIFIED ADDITIONAL COSTS AMOUNTING TO 12 CENTS PER TON.

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HE ALSO INDICATED THAT GOP WAS PREPARED TO ACCEPT DOCUMENT-
ATION PRESENTED BY MARCONA SHOWING HIGHER COSTS.

2. LA ROSA ARGUED AS WELL THAT THE 4 PERCENT ALLOWANCE WAS
PROHIBITED UNDER PERUVIAN LAW WHICH REGULATES INTRA-
COMPANY TRANSFERS. HE CONCEDED THAT GOP HAD ACCEPTED
THIS FORMULA FOR SOME YEARS BUT ARGUED THAT A MISTAKE
EARLIER WHOULD NOT PRECLUDE THE GOP FROM RECTIFYING
THE SITUATION WHEN IT WAS DISCOVERED.

3. FISHLOW CONTENDED THAT THE ESTABLISHMENT OF THE 4
PERCENT ALLOWANCE CREATED PRECISELY THE KIND OF ARMS-LENGTH TRANS-
ACTION WHICH WAS BEHIND THE INTENT OF THE LIMITATIONS IN
PERUVIAN LAW. HAD A COST-PLUS FORMULA BEEN INCORPORATED
IN THE CONTRACT, FISHLOW SAID, MARCONA WOULD HAVE HAD NO
INCENTIVE TO HOLD DOWN THESE MARKETING AND RELATED COSTS.
ON THE OTHER HAND, WITH THE 4 PERCENT LIMITATION MARCONA WAS RE-
QUIRED TO MAINTAIN AN EFFICIENT OPERATION, THEREBY KEEPING
COSTS TO A MINIMUM. FISHLOW ALSO WELCOMED LA ROSA'S
CONSTRUCTIVE PROOSAL (REGARDING ESTABLISHMENT OF COSTS)
AS A POSITIVE STEP TOWARD RESOLUTION OF THIS MAJOR TAX CLAIM.
INGERSOLL

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